

**Tennessee Board of Regents
Endowment for Educational Excellence
Tennessee State University Foundation**

For the Year Ended June 30, 2004

Arthur A. Hayes, Jr., CPA, JD, CFE
Director

Charles K. Bridges, CPA
Assistant Director

Shirley A. Henry, CPA
Audit Manager

Keith Isbell
In-Charge Auditor

Tiffany Cherry, CFE
Staff Auditor

Gerry Boaz, CPA
Technical Analyst

Amy Brack
Editor

Comptroller of the Treasury, Division of State Audit
1500 James K. Polk Building, Nashville, TN 37243-0264
(615) 401-7897

Financial/compliance audits of colleges and universities are available on-line at
www.comptroller.state.tn.us/sa/reports/index.html.
For more information about the Comptroller of the Treasury, please visit our Web site at
www.comptroller.state.tn.us.



STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
State Capitol
Nashville, Tennessee 37243-0260
(615) 741-2501

John G. Morgan
Comptroller

January 20, 2005

The Honorable Phil Bredesen, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and

The Honorable Charles W. Manning, Chancellor
Tennessee Board of Regents
1415 Murfreesboro Road, Suite 350
Nashville, Tennessee 37217
and

Dr. James A. Hefner, President
Tennessee State University
3500 John A. Merritt Boulevard
Nashville, Tennessee 37209

Ladies and Gentlemen:

Transmitted herewith is the report on the Endowment for Educational Excellence at the Tennessee State University Foundation for the year ended June 30, 2004. The audit was conducted under the requirements of the trust agreement which established the endowment. You will note from the independent auditor's report that an unqualified opinion was given on the fairness of the presentation of the financial statements.

Sincerely,

John G. Morgan
Comptroller of the Treasury

JGM/sah
05/031



**STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT
SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-0264
PHONE (615) 401-7897
FAX (615) 532-2765**

Independent Auditor's Report

November 12, 2004

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

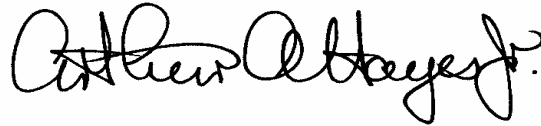
We have audited the accompanying statement of net assets of the Endowment for Educational Excellence at the Tennessee State University Foundation as of June 30, 2004, and the related statement of revenues, expenses, and changes in net assets for the year then ended. These financial statements are the responsibility of the foundation's management. Our responsibility is to express an opinion on these financial statements, based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The Honorable John G. Morgan
November 12, 2004
Page Two

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Endowment for Educational Excellence at the Tennessee State University Foundation as of June 30, 2004, and the changes in financial position for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Sincerely,

A handwritten signature in black ink, reading "Arthur A. Hayes, Jr." in a cursive script.

Arthur A. Hayes, Jr., CPA
Director

AAH/sah

**TENNESSEE BOARD OF REGENTS
 ENDOWMENT FOR EDUCATIONAL EXCELLENCE
 TENNESSEE STATE UNIVERSITY FOUNDATION
 STATEMENT OF NET ASSETS
 JUNE 30, 2004**

ASSETS

Current assets:

Accrued interest receivable	\$ 10,656.65
Total current assets	<u>10,656.65</u>

Noncurrent assets:

Cash and cash equivalents (Notes 2 and 3)	4,919,856.31
Investments (Note 4)	<u>4,231,066.35</u>
Total noncurrent assets	<u>9,150,922.66</u>
Total assets	<u>9,161,579.31</u>

NET ASSETS

Restricted for:

Nonexpendable:

Scholarships and fellowships	9,161,579.31
Total net assets	\$ <u><u>9,161,579.31</u></u>

The notes to the financial statements are an integral part of this statement.

**TENNESSEE BOARD OF REGENTS
 ENDOWMENT FOR EDUCATIONAL EXCELLENCE
 TENNESSEE STATE UNIVERSITY FOUNDATION
 STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
 FOR THE YEAR ENDED JUNE 30, 2004**

NONOPERATING REVENUES (EXPENSES)

State appropriations	\$ 1,000,000.00
Gifts	121,754.92
Grants and contracts	1,762,878.00
Investment income	94,373.59
Other nonoperating revenues (expenses)	112,540.38
Net nonoperating revenues	<u>3,091,546.89</u>
Increase in net assets	<u>3,091,546.89</u>

NET ASSETS

Net assets - beginning of year	<u>6,070,032.42</u>
Net assets - end of year	<u>\$ <u>9,161,579.31</u></u>

The notes to the financial statements are an integral part of this statement.

**Tennessee Board of Regents
Endowment for Educational Excellence
Tennessee State University Foundation
Notes to the Financial Statements
June 30, 2004**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

Pursuant to the consent decree entered into on January 5, 2001, in settlement of the Geier v. Sundquist lawsuit, the Tennessee State University Endowment for Educational Excellence trust was established. This trust was created by the Tennessee Board of Regents and is operated exclusively for the educational purposes at Tennessee State University. The Tennessee State University Foundation is the trustee of these funds and, in accordance with the trust agreement, delegates the actual management of the endowment assets to professional investment managers. These assets are the property of the State of Tennessee.

Basis of Presentation

The financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

Basis of Accounting

The financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The foundation has the option of following private-sector guidance issued subsequent to November 30, 1989, subject to the above limitation. The foundation has elected not to follow private-sector guidance issued subsequent to November 30, 1989.

The endowment's activity is nonoperating in nature and includes (1) state appropriations provided as a part of the consent decree, (2) federal grant funds from the U.S. Department of Education under the Title III Strengthening Historically Black Colleges and Universities Program, (3) investment income, and (4) gifts.

**Tennessee Board of Regents
Endowment for Educational Excellence
Tennessee State University Foundation
Notes to the Financial Statements (Cont.)
June 30, 2004**

Net Assets

The endowment's net assets are classified as nonexpendable restricted net assets. Nonexpendable restricted net assets consist of endowment and similar type funds in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may be expendable or added to principal. The trust agreement does provide for spending a portion of the income, as discussed in Note 5. Spending decisions are to be made by the Budget Committee established in the trust agreement through the preparation of an annual budget. However, as of June 30, 2004, no funds have been designated to be spent.

NOTE 2. CASH AND CASH EQUIVALENTS

In addition to demand deposits, this classification includes instruments which are readily convertible to known amounts of cash and which have original maturities of three months or less. At June 30, 2004, cash and cash equivalents consisted of \$32,584.75 in bank accounts and \$4,887,271.56 in capital management account money funds.

NOTE 3. DEPOSITS

Some of the foundation's deposits are in financial institutions that participate in the bank collateral pool administered by the State Treasurer. The securities pledged to protect these accounts are pledged in the aggregate rather than against each individual account. The members of the pool may be required by agreement to pay an assessment to cover any deficiency. Under this additional assessment agreement, public fund accounts covered by the pool are considered to be insured for purposes of credit risk disclosure.

The laws of the State of Tennessee require that collateral be pledged to secure all uninsured deposits. Tennessee Board of Regents policies require that the market value of collateral pledged equal 115%, 100%, or 90% of the uninsured deposits at financial institutions participating in the collateral pool. The pledge level is based on

**Tennessee Board of Regents
Endowment for Educational Excellence
Tennessee State University Foundation
Notes to the Financial Statements (Cont.)
June 30, 2004**

financial criteria set by the Collateral Pool Board with the financially strongest institutions being eligible for the lowest pledge level.

Deposits with financial institutions are required to be categorized to indicate the level of risk assumed by the foundation. Category 1 consists of deposits that are insured or collateralized with securities held by the foundation or by its agent in the foundation's name. Category 3 deposits are uncollateralized. This category includes any bank balance that is collateralized with securities held by the pledging financial institution or by its trust department or agent but not in the foundation's name.

At June 30, 2004, the carrying amount of the endowment's portion of the foundation's deposits was \$2,976,165.48, and the bank balance was \$2,976,165.48. Of the bank balance, \$1,299,276.89 was category 1, and \$1,676,888.59 was category 3.

NOTE 4. INVESTMENTS

The trust agreement requires that the foundation delegate the actual management of the endowment assets to one or more professional investment managers, which are to be selected on the basis of demonstrated performance, management philosophy, investment style, and fees. As of June 30, 2004, the endowment assets were under the management of three banks and one investment company. The foundation is authorized to invest the endowment funds in accordance with the trust agreement. Under the trust agreement, the foundation is authorized to invest and reinvest the property of the trust in any kind of real and/or personal property and any kind of investment specifically including, but not limited to, domestic or foreign government obligations of any kind; domestic or foreign securities of any kind including, but not limited to, preferred or common stocks, bonds, mortgage participations and shares of investment trusts, investment companies, money market funds, mutual funds (including market or index funds); options to purchase or sell domestic or foreign securities or domestic or foreign government obligations of any kind; and interests in partnerships, so long as such investments are made with the care of a fiduciary.

All investments permitted to be reported at fair value under GASB Statement 31 are reported at fair value, including those with a maturity date of one year or less at the time of purchase.

**Tennessee Board of Regents
Endowment for Educational Excellence
Tennessee State University Foundation
Notes to the Financial Statements (Cont.)
June 30, 2004**

The foundation's investments related to the endowment are categorized below to indicate the level of risk assumed by the foundation at year-end. Category 2 consists of uninsured and unregistered investments for which the securities are held by the counterparties' trust department or agent in the foundation's name.

Category 2:

U.S. government securities	\$ 799,236.60
Corporate bonds	1,060,367.00
Corporate stocks	1,917,805.30
Mortgage backed securities	167,329.15

Investments not susceptible to credit risk categorization:

Mutual funds	<u>286,328.30</u>
--------------	-------------------

Total	<u>\$ 4,231,066.35</u>
-------	------------------------

NOTE 5. ENDOWMENT INCOME

The trust agreement requires that at least 25% of the annual income be added to the corpus and stipulates approved and prohibited uses of the other 75%. The grant agreement for the Title III program requires that 50% of the income be added to the corpus and has provisions on the allowable uses of the other 50%. As of June 30, 2004, none of the investment income has been spent.